



**COUNTY OF LOS ANGELES  
DEPARTMENT OF AUDITOR-CONTROLLER**

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March 22, 2010

TO: Supervisor Gloria Molina, Chair  
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FROM: Wendy L. Watanabe  
Auditor-Controller

William T Fujioka  
Chief Executive Officer

SUBJECT: **MARCH 23, 2010 BOARD AGENDA ITEM #13**

In the last few days, two County employees sent e-mails to your Offices encouraging Board members to vote no on Item 13, on Tuesday, March 23, 2010. We want to inform you that both e-mails have factual errors and overstated the net impact to employees. These two e-mails neglected to disclose that the employees must pay the additional income tax liability, sooner or later. Employee payroll taxes are the responsibility of the employees and it cannot be avoided.

**An Additional Pay-Period and Financial Impact to Employees**

It is true that under the new eHR Payroll System, employees will be impacted financially, one-time, because there will be an extra pay-period reported on employees' W-2 Forms for 2010. This impact is due to aligning employees' earnings with income reporting periods. It has been a long-standing practice, under the old payroll system, that the first half of December earnings are reported as paid in the following tax year. For an individual, this started the first year the employee was hired by the County and occurs each year until the employee leaves County service. During that first year and each following year, the employee's first half of December earnings are reported the following year.

The new semi-monthly Payroll System will more closely align the payment of an employee's earnings with the income reporting period. It will also appropriately report those earnings in the correct tax year based on semi-monthly rather than monthly earnings. The new system will correctly reflect the employee's semi-monthly earnings on the 2010 W-2 Form (distributed in January 2011).

However, regardless of the new semi-monthly Payroll System, all employees will be taxed for this additional pay-period, whether it is now with the implementation of the new Payroll System, or later when employees leave County service. The new eHR Payroll System accelerates the inevitable tax consequences to the employees and deals with the unavoidable additional employee tax liability.

### **Full Disclosure**

We have fully disclosed and communicated to all employees that **reporting** an extra half month earnings during 2010 will impact their State and Federal tax liability. We informed all employees to consider adjusting their 2010 income tax withholding to compensate for the added one-time tax liability.

Between December 2009 and present, we communicated through various mechanisms including Information Flyers, Frequently Asked Questions (FAQs) on the County website, departmental training, and many discussions or meetings with the labor unions. Specifically, Flyer #1 and #8 were distributed to all County employees on January 15 and March 15, 2010, respectively and addressed the impact the additional pay-period in 2010 will have on employees.

Flyer #1 clearly says that "...there will be an extra pay-period reported to the IRS and the State for the 2010 tax year. The one-time conversion from monthly to semi-monthly pay-periods will result in 12 ½ months of taxable earnings reported on an employee's W-2 Form for the 2010 tax year (issued in January 2011). This is caused by inclusion of the first half of December 2010 earnings in the December 30, 2010 pay check". Flyer #8 indicates that "For most employees, the change in 2010 State and Federal Tax liability will be greater than additional taxes withheld due to the extra pay-period. You may want to consider adjusting your withholding allowances, status, or have an additional amount withheld each semi-monthly pay-period to compensate for this".

Lastly, the FAQs state that employees "...may wish to consult with a tax specialist" regarding withholding additional incomes taxes in 2010 to compensate for the potential additional tax liability. It would be inappropriate for the Auditor-Controller's Office to provide specific tax advice to employees, as we are not tax advisors.

### **Ranges of Impact to Employee**

An additional pay-period reported means additional payroll taxes withheld. The W-2 Form will show a higher taxable income and additional tax withholdings than what would have been shown under the old payroll system. Although additional taxes will be withheld, the amount may not equate to the employee's actual tax liability when filing 2010 taxes. The exact impact to County employees is solely dependent upon their particular tax circumstances (i.e., single, married, other income, etc.).

Both e-mails indicated the tax impact to be \$530 to \$700 for average County employees. However, their estimates omit the fact that the additional withholding will also be reported on the W-2 Form to offset the tax consequences to the employees. We estimated the net impact for the average employee to be approximately \$300 for the year, conservatively using the single-person tax table.

### **Coordination Efforts with Labor Unions**

Throughout 2009 to present, meetings with employee representatives from the Coalition of County Unions (CCU) and SEIU Local 721 (SEIU) were regularly held on the new payroll system. In these meetings, we provided implementation status with explanations of the recommended policy changes, including the one-time effect of converting from a monthly payroll system to a semi-monthly, e.g., the additional pay-period of taxable earnings in 2010.

Please call us if you have any additional questions.

WTF:WLW:MMO:RAD:GI

c: County Counsel  
Department of Human Resources